Supreme Court, U.S.
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No. 95-951

In The

Supreme Court of the United States

October Term, 1995

LESLIE U. HARRIS, On Behalf of Himself and All Others Similarly Situated,

Petitioner,

v.

CHASE MANHATTAN BANK, N.A. And DOES 1 THROUGH 50,

Respondents.

On Petition For A Writ Of Certiorari To The Supreme Court Of California

RESPONDENTS' BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Section 27 of the Federal Deposit Insurance Act, 12 U.S.C. §1831d, and Section 85 of the National Bank Act, 12 U.S.C. §85, authorize federally-insured state banks and national banks, respectively, to charge on their intrastate and interstate loans the "interest" allowed by the laws of their home States. The question presented is:

Whether the meaning of the term "interest" in Section 27 of the Federal Deposit Insurance Act and Section 85 of the National Bank Act is narrowly confined to percentage-based periodic interest rates, as held by the New Jersey Supreme Court, or also encompasses a flat late charge that a borrower has agreed to pay in the event of delinquency, as held by the Courts of Appeals for the First and Third Circuits and the Supreme Courts of California and Colorado?

Petitioner's "Questions Presented" are inaccurate insofar as they suggest that this case involves only Section 85 of the National Bank Act. During the period of time covered by the Complaint, Respondent The Chase Manhattan Bank (USA) converted its charter from a national bank to a federally-insured state bank. Therefore, this case involves Section 85 of the National Bank Act and Section 27 of the Federal Deposit Insurance Act.

Also, the second of Petitioner's "Questions Presented," which purports to raise a constitutional issue regarding delegation of Congressional powers, is procedurally improper because it was not raised in the courts below by Petitioner and has not been briefed in the Petition for a Writ of Certiorari.

RULE 29.6 STATEMENT

Respondents are The Chase Manhattan Bank (USA) and The Chase Manhattan Bank, N.A. Both Respondents are wholly owned by The Chase Manhattan Corporation. The Chase Manhattan Bank (USA) does not have any nonwholly owned subsidiaries. The first-tier nonwholly owned subsidiaries of The Chase Manhattan Bank, N.A. are 15253 Bake Parkway; Chase Automated Clearing House, Inc.; Corporation Falcon, Inc.; Credit Martiniquais; Electronic Payment Service Company (Hong Kong) Ltd.; Monthly Gyde, Inc.; Pantherhaven Limited; Societe de Developpement Regional Antilles; Superior One; and VCI, PLC.

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OPINIONS BELOW

The Order of the California Supreme Court dismissing review is published as *Harris v. Chase Manhattan Bank, N.A.*, 905 P.2d 417, 46 Cal.Rptr.2d 748 (Cal. Nov. 2, 1995) and is reprinted in Petitioner's Appendix at A-34. The Order of the California Supreme Court which previously granted review is published as *Harris v. Chase Manhattan Bank, N.A.*, 889 P.2d 540, 38 Cal.Rptr.2d 346 (Cal. Feb. 23, 1995) and is reprinted in the Petitioner's Appendix at A-33. The opinion of the Court of Appeal appears at *Harris v. Chase Manhattan Bank, N.A.*, 34 Cal. App.4th 1563, 35 Cal.Rptr.2d 733 (1994) and is reprinted in the Petitioner's Appendix at A-20 to A-32. The order of the trial court is not reported and is reprinted in the Petitioner's Appendix at A-18 to A-20.

JURISDICTION

The California Supreme Court entered its judgment on November 2, 1995. The petition was filed and docketed on December 18, 1995. The jurisdiction of this Court is invoked under 28 U.S.C. §1257(a).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Supremacy Clause, U.S. Const. art. VI, cl. 2, is set out at page 3 of the petition.

Section 85 of the National Bank Act, 12 U.S.C. §85, is set out, in pertinent part, at pages 3-4 of the petition.

Section 27 of the Federal Deposit Insurance Act, 12 U.S.C. §1831d(a), provides in pertinent part:

> In order to prevent discrimination against State-chartered insured depository institutions . . . such State bank . . . may, notwithstanding any State constitution or statute which is hereby preempted for the purposes of this section, take, receive, reserve, and charge on any loan or discount made, or upon any note, bill of exchange, or other evidence of debt, interest . . . at the rate allowed by the laws of the State, territory, or district where the bank is located . . .

Section 950 of Title 5 of the Delaware Code is set out at page 6 of the petition.

Section 1671 of the California Civil Code is set out at pages 4-5 of the petition.

STATEMENT OF THE CASE

A. INTRODUCTION

Respondents The Chase Manhattan Bank (USA) and The Chase Manhattan Bank, N.A. submit this Brief to express their agreement with petitioner that the Court should grant a writ of certiorari to resolve a direct conflict between the Supreme Courts of California and Colorado and the First and Third Circuit Courts of Appeals, on the one hand, and the New Jersey Supreme Court, on the other, on a federal banking law issue of enormous importance to federally-insured depository institutions throughout the country.

The First and Third Circuits and the highest courts of California and Colorado have held that the term "interest" in Section 27 of the Federal Deposit Insurance Act ("FDIA"), 12 U.S.C. §1831d, and/or Section 85 of the National Bank Act ("NBA"), 12 U.S.C. §85, encompasses not only percentage-based periodic rates, but also flat late charges. *Harris v. Chase Manhattan Bank, N.A.*, 34 Cal. App.4th 1563, 35 Cal.Rptr.2d 733 (1994) (Section 27 and Section 85), *review granted*, 889 P.2d 540, 38 Cal.Rptr.2d 346 (Cal. 1995), *review dismissed*, 905 P.2d 417, 46 Cal.Rptr.2d 748 (Cal. 1995), *petition for certiorari pending*, No. 95-951 (U.S. Dec. 18, 1995); *Spellman v. Meridian Bank (Delaware)*, Nos. 94-3203, 3204, 3215-18, 1995 U.S. App. LEXIS 37149 at *56 to *68 (3d Cir. Dec. 29, 1995) (Section 85); *Greenwood Trust Co. v. Massachusetts*, 971 F.2d 818 (1st Cir. 1992) (Section 27), *cert. denied*, 113 S. Ct. 974 (1993); *Smiley v. Citibank (South Dakota), N.A.*, 11 Cal. 4th 138, 44 Cal.Rptr.2d 441, 900 P.2d 690 (1995) (Section 85), *petition for certiorari pending*, No. 95-860 (U.S. Nov. 30, 1995); *Stoorman v. Greenwood Trust Co.*, No. 94SC382, 1995 Colo. LEXIS 764 (Colo. Dec. 18, 1995) (Section 27); *Copeland v. MBNA America Bank, N.A.*, No. 94SC409, 1995 Colo. LEXIS 743 (Colo. Nov. 20, 1995) (Section 85), *petition for certiorari pending*, No. 95-1056 (U.S. Dec. 28, 1995); *Richardson v. Citibank (South Dakota), N.A.*, No. 94SC670, 1995 Colo. LEXIS 767 (Colo. Dec. 18, 1995) (Section 85).

However, the Supreme Court of New Jersey has expressly disagreed with the foregoing rulings, and instead has held that the meaning of "interest" in Section 27 of the FDIA and Section 85 of the NBA is limited to percentage-based periodic rates. *Hunter v. Greenwood Trust Co.*, No. A-103-94, 1995 N.J. LEXIS 1354 (N.J. Nov.

28, 1995) (Section 27), *petition for certiorari pending*, No. 95-963 (U.S. Dec. 18, 1995); *Sherman v. Citibank (South Dakota), N.A.*, No. A-102-94, 1995 N.J. LEXIS 1355 (N.J. Nov. 28, 1995) (Section 85), *petition for certiorari pending*, No. 95-991 (U.S. Dec. 21, 1995).

Unlike any of the other cases now pending before this Court, this case involves *both* Section 85 of the NBA *and* Section 27 of the FDIA. For the first two years of the four-year period covered by the Complaint, Respondent The Chase Manhattan Bank (USA) ("Chase") was a national bank governed by Section 85 of the NBA. For the remaining two years of the relevant period, Chase was a federally-insured state bank governed by Section 27 of the FDIA.

Certiorari is warranted not only because of the conflicts in the courts below, but also because of the profound national importance of the federal banking law issue involved. This Court has never construed the term "interest" in Section 27 of the FDIA and Section 85 of the NBA or the other two similarly-worded banking statutes (12 U.S.C. §1463(g) and 12 U.S.C. §1785(g)), and the proper interpretation of these statutes is of critical importance since they govern all types of intrastate and interstate lending by national banks and federally-insured state banks, savings associations, and credit unions. Indeed, the proper interpretation of "interest" is necessary to ensure the continued vitality of the "most favored lender" doctrine enunciated by this Court over a century ago in *Tiffany v. National Bank of Missouri*, 85 U.S. (18 Wall.) 409 (1874), which mandates that national banks and federally-insured state banks be afforded competitive equality with other lenders located in the same state.

This case may affect the interstate exportation not just of late charges, but also other fees customarily imposed by credit card issuers and other lenders, such as annual fees, overlimit fees, and cash advance fees. This case has nationwide significance since numerous states' laws prohibit or limit late charges and other of the foregoing fees. Moreover, with over $3 billion in fee revenue (*i.e.*, revenue not derived from periodic finance charges) collected each year by credit card issuers, the federal banking law issue presented here has enormous ramifications for the entire credit card industry. It will determine credit card issuers' potential liability for transactions completed in prior years, and will also affect their current and future lending practices. The resolution of this issue will also have a major impact on other types of intrastate and interstate lending as well.

Given the tremendous disruption and uncertainty for the banking industry, federal banking agencies, state legislatures and borrowers that has been created by the direct conflicts in the courts below, it is vital that guidance be provided by this Court.

B. FACTUAL BACKGROUND

Until June 21, 1990, The Chase Manhattan Bank (USA) ("Chase") was a national banking association chartered by the Comptroller of the Currency ("OCC") and located in Delaware. Since that time, it has been a

federally-insured state-chartered bank located in Delaware. (A-21).[1]

As part of its banking services, Chase issues VISA and MasterCard credit cards, pursuant to which it lends money on an open-end credit basis to borrowers throughout the United States. The terms and conditions governing the use of the credit cards are set forth in the written Agreement provided to cardmembers when they receive their cards.

Petitioner is a California citizen who holds a Chase MasterCard. He has challenged a provision in the cardmember agreement authorizing Chase to impose a $10 late charge if the cardmember fails to make timely payment of the required minimum monthly balance. Chase imposes its late charge on an interstate basis in reliance upon Section 27 of the FDIA, which authorizes a federally-insured state bank to charge "interest" on its loans at "the rate allowed by the laws of the State . . . where the bank is located," and expressly provides that any contrary law in the borrower's State "is hereby preempted." For the period when Chase was a national bank, it imposed its late charge on an interstate basis in reliance upon Section 85 of the NBA, which authorizes a national bank to charge "interest" on its loans "at the rate allowed by the laws of the State . . . where the bank is located . . . " Chase is located in Delaware, whose laws

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[1] Respondent The Chase Manhattan Bank, N.A. is a nominal defendant in this case, inasmuch as it was stipulated below that it did not issue any credit cards during the relevant time period.

authorize the imposition of any late charge agreed to between a borrower and a lender. Del. Code Ann., Title 5, §950.

C. PROCEDURAL HISTORY

Petitioner Leslie Harris filed this putative class action on March 6, 1992 on behalf of himself and all other California residents who had been issued a VISA or MasterCard credit card by Chase and were assessed a late charge. He alleged that the late charge constituted a liquidated damages penalty in violation of Section 1671 of the California Civil Code and also violated the California Unfair Trade Practices Act, Cal. Bus. & Prof. Code §§17200 *et seq.* (A-1 to A-17).

This case is one of numerous class actions filed around the country against the nation's leading credit card issuers in the wake of a decision by a District Court in Massachusetts holding that late charges are not "interest" under Section 27 of the FDIA and that Massachusetts' statutory prohibition of late charges was not preempted. *Greenwood Trust Co. v. Massachusetts*, 776 F.Supp. 21 (D. Mass. 1991). However, after this case and the many others like it were commenced, the Court of Appeals for the First Circuit unanimously reversed the District Court's decision, and this Court denied Massachusetts' Petition for a Writ of Certiorari. *Greenwood Trust Co. v. Massachusetts*, 971 F.2d 818 (1st Cir. 1992), *cert. denied*, 113 S. Ct. 974 (1993).

On February 3, 1993, the trial court granted Chase's general demurrer to the Amended Complaint on the

ground that petitioner's claims were preempted by Section 27 of the FDIA (for the time period since Chase became a federally-insured state bank) and Section 85 of the NBA (for the time period when Chase had been a national bank).[2] (A-18 to A-20).

On November 17, 1994, the California Court of Appeal unanimously affirmed the order of dismissal, holding that petitioner's claims were preempted by Section 27 of the FDIA and Section 85 of the NBA. *Harris v. Chase Manhattan Bank N.A.*, 34 Cal. App.4th 1563, 35 Cal.Rptr.2d 733 (1994) (A-20 to A-32).

The Court of Appeal expressly agreed with the reasoning of the First Circuit Court of Appeals in *Greenwood Trust v. Massachusetts*, and held that Section 27 of the FDIA and Section 85 of the NBA "preempt contrary state laws regulating late charges and other flat fees in connection with credit card lending." 34 Cal. App.4th at 1571. The Court held that "given the unmistakable intent of Congress to level the playing field and create lending parity between state and national banks" when Section 27 of the FDIA was enacted in 1980, along with the fact that Section 27 "borrowed language extensively from section 85," the term "interest" in both statutes should be interpreted the same way. *Id.* at 1570, 1574. The Court cited numerous cases demonstrating that "even before the

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[2] Petitioner's claims covered a four-year period from March 6, 1988 to the date the complaint was filed, March 6, 1992. (A-4). As stated above, Chase converted from a national bank to a state bank in June, 1990.

enactment of section 521 [Section 27 of the FDIA],[3] federal courts had consistently construed the term 'interest' in section 85 to embrace not only periodic percentage rates but a host of other fees incidental to the loaning or forbearance of money."[4] *Id.* at 1571-1572. The Court reasoned as follows:

> In lifting section 85's language and engrafting it onto section 521, Congress is presumed to have been aware of prior judicial decisions interpreting the older statute (*Holmes v. SIPC* (1992) ___ U.S. ___ [117 L.Ed.2d 532, 543-544, 112 S. Ct. 1311, 1317-1318]), including the courts' sweeping construction of the term 'interest.' . . . Viewed from this historical perspective, Congress's intent to define 'interest' in the broadest sense for preemption purposes could not be more clear. 34 Cal. App. 4th at 1572.

The Court of Appeal accorded deference to the views of the OCC and Federal Deposit Insurance Corporation ("FDIC"), which have opined that late charges are within

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[3] Section 27 of the FDIA originated as Section 521 of the Depository Institutions Deregulation and Monetary Control Act of 1980 ("DIDA"), Pub. L. No. 96-221, 94 Stat. 132 (March 31, 1980).

[4] Similarly, in the Third Circuit's very recent decision in *Spellman v. Meridian Bank (Delaware)*, Nos. 94-3203, 3204, 3215-18, 1995 U.S. App. LEXIS 37149 at *63-*64 (3d Cir. Dec. 29, 1995), the Court cited numerous older precedents demonstrating that "the significant weight of authority" comports with an expansive definition of "interest" in Section 85, and these cases "recognize that various loan charges often are substantively similar in their economic function to the periodic percentage rates casually termed 'interest.' "

the preemptive scope of Section 85 of the NBA and Section 27 of the FDIA, respectively.[5] *Id.* at 1571. the Court also stated that late charges fall within the dictionary definition of "interest" as "compensation allowed by law or fixed by the parties for the use or forbearance or detention of money." *Id.* at 1573 n. 2, quoting *Black's Law Dictionary* (5th ed. 1979) p. 729. The Court explained that "[t]he cardholder who is late in tendering the minimum monthly payment enjoys use of that money in the meantime and the late charge compensates the lender for such forbearance." 34 Cal. App. 4th at 1573 n. 2.

On February 23, 1995, the California Supreme Court granted review of the Court of Appeal's decision. 889 P.2d 540, 38 Cal.Rptr.2d 346. (A-33). However, on November 2, 1995, after the California Supreme Court rendered its decision in favor of the defendant bank in *Smiley v. Citibank, supra,* it dismissed its prior order of review

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[5] The FDIC has specifically concluded that credit card late charges imposed by federally-insured state banks are "interest" under Section 27 of the FDIA. FDIC Op. No. 92-47, [1992-1993 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,534 (July 8, 1992). The OCC likewise has opined on several occasions that credit card late charges are "interest" under Section 85 of the NBA. OCC Interpretive Ltr. No. 670, [1994-1995 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,618 (Feb. 17, 1995); Letter from William P. Bowden, Jr., OCC Chief Counsel, 1992 WL 136390 (OCC) (Feb. 4, 1992); OCC Interpretive Ltr. No. 452, [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,676 (Aug. 11, 1988). *See also* 60 Fed. Reg. 11924, 11940 (March 3, 1995) (proposed OCC Interpretive Ruling stating that late charges are "interest" under Section 85).

in this case as improvidently granted. 905 P.2d 417, 46 Cal.Rptr.2d 748. (A-34).

ARGUMENT

A. There Exists a Direct Conflict in the Courts Below Concerning the Meaning of "Interest" in Section 27 of the FDIA and Section 85 of the NBA

Chase agrees with petitioner that this Court should grant a writ of certiorari to resolve a sharp and direct conflict in the courts below concerning the meaning of "interest" in Section 27 of the FDIA and Section 85 of the NBA. This case involves *both* of those statutes.

The highest courts of California and Colorado, along with the First and Third Circuit Courts of Appeals, have all held that late charges are "interest" for purposes of Section 27 of the FDIA and/or Section 85 of the NBA. *See* p. 3, *supra*. However, the New Jersey Supreme Court rendered a contrary holding in *Hunter v. Greenwood Trust Co.* (Section 27) and *Sherman v. Citibank* (Section 85). Moreover, other cases involving the issue of whether credit card late charges are "interest" under the federal banking statutes are pending in other jurisdictions and also have reached conflicting conclusions.[6]

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[6] A lower court held that credit card late charges are "interest" under Section 85 of the NBA in *Tikkanen v. Citibank, N.A.*, 801 F.Supp. 270 (D. Minn. 1992). The only court besides the New Jersey Supreme Court to conclude that credit card late charges are not "interest" under federal law is the intermediate

The pressing need for Supreme Court resolution of the conflicts in the courts below is vividly illustrated by the sharp conflicts now existing within the Third Circuit itself regarding the question of whether late charges are "interest" under Section 85 of the NBA and Section 27 of the FDIA. Although the Third Circuit has answered that question in the affirmative, directly contrary decisions were previously rendered by the New Jersey Supreme Court and by the intermediate appellate court in Pennsylvania. *See* n. 6, *supra*.

Thus, for banks and borrowers who are located in or doing business in New Jersey and Pennsylvania, the meaning of "interest" in Section 27 of the FDIA and Section 85 of the NBA turns solely on the happenstance of whether suit is brought in federal court or state court. By the same token, national credit card issuers such as Chase are also confronted with conflicts on a national level concerning the legality of their interstate exportation of late charges – while that practice has been judicially approved by the First Circuit, Third Circuit, and the highest courts of California and Colorado, it has been

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appellate court in Pennsylvania, and that court's decision has been granted review by the Pennsylvania Supreme Court. *Mazaika v. Bank One, Columbus, N.A.*, 439 Pa. Super. 95, 653 A.2d 640 (1994) (*en banc*), *allocatur granted*, 659 A.2d 557 (Pa. May 25, 1995); *In re: Citibank (South Dakota) Credit Card Litigation*, 439 Pa. Super. 79, 653 A.2d 39 (1995), *allocatur granted*, 659 A.2d 984 (Pa. May 31, 1995); *Gadon v. The Chase Manhattan Bank (USA)*, 439 Pa. Super. 210, 653 A.2d 697 (1995) (appeal pending). In addition to the foregoing cases, there are many other cases pending around the country against credit card issuers in which published decisions have not been rendered.

declared illegal by the New Jersey Supreme Court and Pennsylvania intermediate appellate court.

When this Court denied certiorari in *Greenwood Trust v. Massachusetts* in January, 1993 (113 S. Ct. 974), the issue was still one of first impression in the appellate courts and no conflicts had yet arisen. However, the cases spawned by the reversed District Court decision in *Greenwood Trust v. Massachusetts* have now proceeded through various state Supreme Courts, and a stark conflict has arisen that can be resolved only by this Court. The New Jersey Supreme Court decisions against the banks, like the District Court decision in *Greenwood Trust v. Massachusetts*, undoubtedly will give rise to many more class action lawsuits around the country against federally-insured depository institutions, and these cases will impose substantial burdens and expenses upon the parties and the courts. Unless certiorari is granted now, the conflicting interpretations of the federal banking statutes surely will persist and multiply. These conflicting rulings already have created considerable turmoil and uncertainty for the nation's banking industry and exposed it to potentially enormous damage claims. The longer the conflicts are allowed to continue, the greater the harm that will be inflicted upon the countless lenders and borrowers[7] who participate in the country's multi-billion dollar interstate lending market.

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[7] As a result of the New Jersey Supreme Court's rulings, various federally-insured depository institutions may refrain from imposing late charges on delinquent customers in states that prohibit or limit those charges. Lacking late charges as a means to recoup the significant losses caused by the delinquent

B. The Interpretation of the Meaning of "Interest" in Section 27 of the FDIA and Section 85 of the NBA Has Profound National Importance

Beyond the conflicts discussed above, there can be no doubt about the tremendous legal and economic importance of the federal question presented by this case. This Court has not yet rendered any opinions construing the meaning of the term "interest" in Section 27 of the FDIA, Section 85 of the NBA or the nearly identically-worded statutes applicable to federally-insured savings associations (12 U.S.C. §1463(g)) and federally-insured credit unions (12 U.S.C. §1785(g)). Since the courts and federal banking agencies have held uniformly that "interest" carries the same meaning in all of these statutes, resolution of the question presented in this case will have significant ramifications for all federally-insured depository institutions.

Twenty-six states have laws that prohibit or restrict late charges,[8] and therefore the construction of the meaning of "interest" in Section 27 of the FDIA and Section 85 of the NBA will affect the imposition of late charges not just in California, but throughout the country. Also, even though late charges are the only fees directly at issue in

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cardholders, credit card issuers may have to raise periodic interest rates for all customers, and may also constrict the availability of credit for individuals of lesser means who are most likely to become delinquent. *See* Dunkelberg, "Litigation Concerning Late Charges is Major Threat to Credit Card Business," Banking Policy Report (April 6, 1992).

[8] DRI/McGraw Hill, *A Study of Employment, Regulations and the Credit Card Industry* at Table 3, pp. 16-18 (Feb. 1993).

this case, the interpretation of the meaning of "interest" in the federal banking laws will affect numerous other fees and charges customarily imposed in connection with credit card loans (*e.g.*, annual fees, overlimit fees, and cash advance fees). Like late charges, these fees have long been "exported" throughout the country by credit card issuers from their home states notwithstanding myriad prohibitions or limitations on these fees in many borrowers' states because they were considered to be charges for the use, forbearance or detention of money that are encompassed within the preemptive scope of the federal banking statutes.[9]

In *Marquette National Bank v. First of Omaha Service Corp.*, 439 U.S. 299 (1978), this Court unanimously held that Section 85 authorized a national bank to "export" the interest allowed by the laws of its home State to credit cardholders in other states with more restrictive usury limits. This Court stressed in *Marquette* that if the meaning of the term "located" in Section 85 of the NBA "were to depend on the whereabouts of each credit-card transaction," this would "throw into confusion the complex system of modern interstate banking." *Id.* at 312. By the

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[9] According to *The New York Times*, "half the states in the country have laws limiting or banning credit card fees for late payments, for annual renewals and for exceeding credit limits." *New York Times*, February 23, 1992 at A1, "Suits Pushing Banks to Obey State Laws on Credit Card Fees." This article includes a chart listing the many states that prohibit late fees, limit late fees, prohibit fees for exceeding a line of credit, and limit annual fees. Although this chart does not reflect legislative changes in a few states since 1992, it nonetheless demonstrates that the issue presented by this case has nationwide repercussions.

same token, if the legality of the late charge imposed by a national credit card issuer such as Chase were to depend on the residence of the cardholder or the whereabouts of each credit-card transaction, the complex system of modern interstate banking would become balkanized and thrown into confusion.

The economic implications of the issue presented here are staggering. According to the most recently available statistics, in 1994 alone the credit card industry received approximately $2.1 billion in revenues from late fees, overlimit fees, and other similar fees; $1.7 billion in annual fees; and $1.3 billion in cash advance fees. Credit Card Management, Card Industry Directory: *The Blue Book of the Credit and Debit Card Industry in the United States,* 1996 ed. at p. 18. The numerous class actions currently pending throughout the country against federally-insured depository institutions that were precipitated by the later-reversed District Court opinion in *Greenwood Trust v. Massachusetts* seek hundreds of millions of dollars in damages under various state consumer protection laws, which typically have statutes of limitation that permit suit for several years of transactions. These lawsuits, along with the new class actions that certainly will be inspired by the New Jersey Supreme Court decisions, may pose a threat to the safety and soundness of the nation's leading financial institutions. Indeed, in an *amicus curiae* brief the FDIC filed in the First Circuit in the *Greenwood Trust v. Massachusetts* case, the agency cautioned that the credit card late charge class actions could "jeopardize the financial integrity of all FDIC-insured institutions."

The meaning of "interest" in the federal banking statutes affects not only credit card lending, but all types of lending. For example, if "interest" were to be construed narrowly to encompass only percentage-based periodic rates, a flat origination fee for a loan might no longer be considered "interest" as a matter of federal law. Also, many states allow flat minimum finance charges on open-end credit, and even though such finance charges clearly constitute "interest," they may not qualify as "interest" under federal banking law if that term is defined in the restrictive manner adopted by the New Jersey Supreme Court. Similarly, flat late charges imposed in connection with home equity loans, automobile loans, and commercial loans would not be "interest" either.

Although this case involves an interstate loan transaction, the construction of the term "interest" will also have a significant impact on intrastate lending by federally-insured depository institutions, since Section 27 of the FDIA and Section 85 of the NBA govern both interstate and intrastate loans. The federal courts and banking agencies have long interpreted "interest" in an expansive manner to include various fees and charges in order to effectuate the "most favored lender" doctrine enunciated by this Court in *Tiffany v. National Bank of Missouri*, 85 U.S. (18 Wall.) 409 (1874), and reiterated a century later in *Marquette*, 439 U.S. at 314 and n. 26. This doctrine provides that, to ensure competitive equality for federally-insured depository institutions and safeguard them from "the hazard of unfriendly legislation by the states," *Tiffany*, 85 U.S. at 413, they are empowered to charge whatever "interest" the "most favored lender" in the

same State is permitted to charge.[10] Federally-insured depository institutions have long relied on the "most favored lender" doctrine in order to "borrow" the more favorable lending authority often bestowed upon other lenders (*e.g.*, credit unions, consumer finance companies, second mortgage loan companies) located in the same State.

If "interest" in Section 27 of the FDIA and Section 85 of the NBA is construed not to include flat fees such as late charges, states may claim a basis for enacting laws enabling certain favored lenders to charge such fees while denying that same right to federally-insured depository institutions, who will no longer be able to invoke the "most favored lender" doctrine to "borrow" the right to charge those fees. This is precisely the type of discrimination against federally-insured depository institutions that the doctrine was intended to prevent.

Indeed, in the Third Circuit's recent decision holding that late charges are "interest" under Section 85 of the NBA, the Court stressed "[t]he most favored lender doctrine and the exportation principle apply to all of a

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[10] Although the "most favored lender" doctrine originally applied only to national banks, the courts and the FDIC have uniformly recognized that, by incorporating the language of Section 85 of the NBA into Section 27 of the FDIA in 1980, Congress conferred "most favored lender" status on federally-insured state banks as well. *Greenwood Trust v. Massachusetts*, 971 F.2d at 826-827; *Smiley v. Citibank*, 11 Cal. 4th at 159; *Hunter v. Greenwood Trust Co.*, 1995 N.J. LEXIS 1354 at *13-*14; *Vanderweyst v. First State Bank*, 425 N.W.2d 803, 806 (Minn.), *cert. denied*, 488 U.S. 943 (1988); FDIC Opinion No. 93-27, [1993-1994 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81,635 (July 12, 1993).

national bank's charges for the use of its money, and the term 'interest' must have a correspondingly broad reach in order to assure parity between national banks and other state lenders." *Spellman v. Meridian Bank (Delaware)*, Nos. 94-3203, 3204, 3215-18, 1995 U.S. App. LEXIS 37149 at *62 (3d Cir. Dec. 29, 1995). The Third Circuit explained that an unduly narrow definition of "interest" would eviscerate the "most favored lender" doctrine:

> A narrower definition would allow states to permit certain favored lenders to assess these charges while denying national banks the same privilege. As Amici for the banks argued in their brief, applying Section 85 only to periodic percentage rates would lead to an unworkable and undesirable hodgepodge of fee limits, and periodic rate provisions, under the laws of both the bank's state and the borrower's state. States often allow lenders to utilize a variety of credit card charges as an integrated package. The Supreme Court noted this point in *Marquette*, 439 U.S. at 302-03, in which it discussed a Nebraska law that set higher percentage rates than did Minnesota law. The Court observed, 'To compensate for the reduced [annual rate of] interest, Minnesota law permits banks to charge annual fees of up to $15 for the privilege of using a bank credit card.' *Id.* Some states could, for example, decide to limit lenders' use of late fees if those lenders are also imposing certain periodic rates. [Plaintiff's] interpretation could therefore result in a borrower in one of these states being subject to the periodic percentage rate limits but not to the limits on other loan charges as well.

Spellman v. Meridian Bank (Delaware), supra, 1995 U.S. App. LEXIS 37149 at *62-*63.[11]

Given the conflicts in the courts below and the enormous sums of money involved, thousands of federally-insured depository institutions throughout the country now find themselves in a difficult quandary as to how to proceed with respect to their credit card and other lending programs. Settled and long-unchallenged interstate and intrastate lending practices have been dramatically disrupted, and a cloud of uncertainty now exists over the legality of billions of dollars in fees and charges collected over the years by credit card issuers and other lenders.

The federal banking law issue presented here affects the entire banking industry, tens of millions of credit card customers, the usury laws of numerous states, and many opinions rendered by the federal banking agencies. Given

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[11] Similarly, the California Supreme Court emphasized that the "most favored lender" doctrine compels a broad definition of "interest:"

> If 'interest' were not read as indicated above [to include late fees], the purpose of facilitating a national banking system by granting national banks 'most favored lender' status in their home states could be frustrated by unfriendly state legislation. Thus, a state could allow periodic percentage charges payable absolutely by maturity for all lenders, *including national banks,* but fix them at a rate so low that they could lend only at a loss. It might then allow late payment fees to some lenders, *not including national banks,* at a level high enough that *they* could lend at a profit. Such a result would be untenable.

Smiley v. Citibank (South Dakota), supra, 11 Cal. 4th at 154 (emphasis in original).

the enormous legal and economic importance of the issues that are presented by this case, Chase agrees with petitioner that certiorari is necessary to provide much-needed guidance to everyone concerned.

CONCLUSION

For the reasons set forth above, Chase agrees with petitioner that this Court should issue a writ of certiorari in this case.

Respectfully submitted,

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